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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1971

No. .....

OZARK AIR LINES, INC.,
Petitioner,

v.

CIVIL AERONAUTICS BOARD.

PETITION FOR A WRIT OF CERTIORARI

To the United States Court of Appeals for the Eighth Circuit

NEALE, NEWMAN, BRADSHAW & FREEMAN
PAUL L. BRADSHAW
705 Woodruff Building
Springfield, Missouri
Counsel for Petitioner

October 29, 1971

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To the United States Court of Appeals for the Eighth Circuit

Petitioner, Ozark Air Lines, Inc., prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Eighth Circuit entered May 5, 1971, affirming an order No. 70-5-107 (Appendix A-6) of the Civil Aeronautics Board made pursuant to rules promulgated under Sec. 406 of the Federal Aviation Act of 1968 (49 U.S.C. 1376(b)) as amended, ordering petitioner to repay $246,579 of subsidy received by Petitioner for Calendar Year 1966, and that on hearing the Court of Appeals' judgment be reversed.

OPINIONS BELOW

The opinion of the Court of Appeals for the Eighth Circuit (Appendix A-6) is reported at 441 F 2d 892.

The opinion of the Civil Aeronautics Board is unreported and is printed here as Appendix A-1.

JURISDICTION

The judgment of the Court of Appeals (Appendix A-6) was entered on May 5, 1971. Timely Motion for Rehearing was filed and was denied on June 2, 1971 (Appendix A-13).

On August 19, 1971, Associate Justice Harry A. Blackmun signed an order extending the time for filing this petition for writ of certiorari to and including October 30, 1971.

The jurisdiction of this Court is invoked under the provisions of 28 U.S.C.A., § 1254 (1).

QUESTIONS PRESENTED

1. Whether the procedure adopted by Respondent for determination of subsidy refunds for 1966 was discriminatory in that the financial data which was utilized by the Respondent to determine Petitioner's liability was not consistent among all the carriers in the class so that any carrier's liability for subsidy refunds was solely dependent upon when a carrier's final subsidy determination was made.

2. Whether Respondent abused its discretion in considering losses reflected by pro forma tax returns filed by Petitioner in 1969, although Section III-E-1 of Class Rate III-A required that losses not reflected in tax returns "Submitted to taxing authorities" not be considered in

determining a refund of subsidy, inasmuch as Petitioner had not "submitted" tax returns to "taxing authorities."

3. Whether Respondent discriminated between Petitioner and Frontier Airlines, Inc. by considering Petitioner's 1969 losses in relation to its subsidy determination for 1966, while not considering a similar loss suffered by Frontier for 1968, where losses for both carriers were known to Respondent at the time it made its respective determinations.

CONSTITUTIONAL, STATUTORY AND RULES PROVISIONS INVOLVED

The Fifth Amendment to the Constitution of the United States provides in pertinent part as follows:

> "No person shall . . . be deprived of life, liberty, or property, without due process of law; . . ."

The Federal Administrative Procedure Act (5 U.S.C. 706), provides in pertinent part as follows:

> "To the extent necessary to decision and when presented, the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of an agency action. The reviewing court shall—
>
> (2) hold unlawful and set aside agency action, findings, and conclusions found to be—
>
> (A) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law;
>
> (B) contrary to constitutional right, power, privilege, or immunity;
>
> (C) in excess of statutory jurisdiction, authority, or limitations, or short of statutory right;"

The Federal Aviation Act (49 U.S.C., § 1376(b)), provides in pertinent part as follows:

> "(b) In fixing and determining fair and reasonable rates of compensation under this section, the Board, considering the conditions peculiar to transportation by aircraft and to the particular air carrier or class of air carriers, may fix different rates for different air carriers or classes of air carriers, and different classes of service. In determining the rate in each case, the Board shall take into consideration, among other factors . . . (3) the need for each such air carrier . . . for compensation . . . sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense."

Section III-E of Civil Aeronautics Board Order E-23850, June 23, 1966, the Board Rules for determining the rate under the Federal Aviation Act (49 U.S.C., § 1376(b)) provides in pertinent part as follows:

> "Federal and State income taxes shall be determined on the basis of the carrier's actual income taxes, including the reducing of taxes resulting from loss carrybacks and carryovers, as reported on its income tax returns submitted to taxing authorities for each year, with such amendments and revisions as may have been filed as of the final determination or profit-sharing hereunder; Provided, however, that, for the purposes of this order, the carrier's actual income taxes for a given review year will be adjusted to exclude taxes related to income which is not other-

wise considered in the profit-sharing determination, hereunder, for that review year; Provided, further, that where a final profit-sharing determination for a prior period has been made and the tax basis relied upon in that final determination has been amended or revised subsequently, the effect of the change in taxes will be considered as income or expense for profit-sharing purposes in the year in which the change is made. . . ."

STATEMENT OF THE CASE

Petitioner is one of nine local service carriers which receive federal subsidy under the Federal Aviation Act of 1968, as amended, 49 U.S.C., § 1376(b). Respondent administers the subsidy program.

The amount of subsidy paid to a carrier is based on such carriers' "need" during a given year, that "need" being determined by a uniform class rate formula. In 1966, the class rate contained a "profit-sharing" provision, requiring a carrier to refund to the Federal Government a portion of its profit for the year in question, as shown by the carrier's income tax return. In 1966, the year in dispute here, the rate was known as Class Rate III-A.

Section III-E-1 of Class Rate III-A provides that tax allowances shall be based upon "tax returns submitted to taxing authorities for each year, with such amendments and revisions as may have been filed as of the final determination of profit-sharing hereunder . . ."

On May 11, 1967, the Respondent's staff made an audit of Petitioner's operations for 1966, based upon certain required forms filed by Petitioner. The staff determined Petitioner's subsidy refund to be $98,788.00, with which figure petitioner was in agreement. On July 22, 1969, the

staff increased this figure to $299,532.00 because of its interpretation of the method used in treating capital gains in computing petitioner's 1968 net operation loss carry-back.

Petitioner protested this determination, and on March 18, 1970, Respondent determined that the staff's determination was erroneous, and that its original figure (98,788.00) was correct. By this time, however, Petitioner's losses for 1969 were evident. The respondent asked for and received, Petitioner's pro forma tax return for 1969, and on the basis of the losses shown therein, the Respondent, in its Order 70-5-107, assessed Petitioner's refund for 1966 at $246,579.00. At the time of Respondent's final determination petitioner had not submitted its 1969 tax return to taxing authorities, having received an extension from the Internal Revenue Service. Therefore, the Respondent's determination admittedly was not, and could not, have been based upon "tax returns submitted to taxing authorities" as provided for in Section III-E-1 of Class Rate III-A.

Other carriers whose subsidy determinations for 1966 were processed earlier in point of time did not have 1969 losses taken into account by Respondent. For example, Respondent determined the "profit sharing" of Frontier Airlines on January 24, 1969. At that time Respondent had before it certain reports showing that Frontier suffered a loss in 1968, and that the loss would be carried back to offset Frontier's 1966 profits. These losses were not considered by the Respondent in its determination of Frontier's 1966 "profit sharing" and it was not required to submit pro forma tax returns for 1968 nor refund any 1966 subsidy.

Petitioner petitioned Respondent to reconsider its order, and upon Respondent's refusal to do so, appealed to the

United States Court of Appeals for the Eighth Circuit. The Court of Appeals affirmed the Respondent's order. The opinion of that Court is set out in Appendix A-6.

The Court of Appeals reasoned that to overturn the Board's order would allow Petitioner to reap a windfall for 1966, noting that inasmuch as Petitioner did not directly compete with the other eight carriers and that "general fairness" prevailed with respect to the Board's treatment, there was no discrimination among the various carriers.

The Court also noted that the Board was justified in ignoring the literal terms of Section III-E-1 inasmuch as, to do otherwise, would "ignore reality" since Petitioner's pro forma tax return showed that a loss carryback would be claimed, notwithstanding the fact that no tax return had been filed with the Internal Revenue Service.

Petitioner seeks review of the decision of the Court of Appeals, and a reversal of its judgment affirming the Respondent's Order No. 70-5-107.

REASONS FOR GRANTING THE WRIT

1. The Respondent's Order No. 70-5-107 is discriminatory and violates the Fifth Amendment of the United States Constitution and Section 10(E) of the Administrative Procedure Act. The Petitioner was required to refund subsidy for 1966 while other airlines similarly situated were not so required. This resulted from the procedure adopted by the Respondent for determining "profit sharing," since there obtained no consistency with respect to the data which would be utilized by the Board to determine any liability to refund subsidy.

The result was that the Respondent utilized 1969 losses in computing the 1966 subsidy for Petitioner, but did not do so for others. In Petitioner's case, the Respondent had the 1969 losses before it only because of the delay resulting from its staff's error in determining Petitioner's 1966 "profit sharing" until after 1969 losses became ascertainable. Thus Petitioner's ultimate liability was the direct result of the order in which its case was processed, there being no uniform date as to when losses would no longer be considered for subsidy purposes.

2. Section III-E-1 of Class Rate III-A contemplates losses reflected by a carrier's tax returns submitted to "taxing authorities." At no time had Petitioner "submitted" its 1969 tax returns to "taxing authorities" and the Respondent's order was based upon a pro forma federal tax return supplied by Petitioner at Respondent's request. With this data in hand, Respondent took the position—as reflected by its order—that by following the clear terms of its own rule, it would, insofar as Petitioner was concerned, "ignore reality."

The Respondent clearly abused its discretion when it disregarded the mandate of its own rule simply because it

did not agree with what the result would be if the unambiguous terms of the rule were to be applied to Petitioner. This is not a case where an administrative agency interpreted its rules. No question of interpretation is involved, as shown by Order No. 70-5-107, and the Respondent made its decision simply because it disapproved of the result that a literal interpretation would necessarily bring.

3. The respondent discriminated between Petitioner and Frontier Airlines in determining subsidy refunds for 1966. Frontier's determination was made on January 27, 1969, and 1969 losses were neither available nor considered. Respondent did, however, know that Frontier had sustained losses in 1968 which would be carried back to offset 1966 profits. Despite its knowledge, Respondent did not take Frontier's 1968 losses into consideration inasmuch as Frontier had not filed its tax return with federal "taxing authorities." The Respondent did not require Frontier to submit pro forma tax returns for 1968, and although certain other reports filed by Frontier indicated a 1968 loss, such loss was not computed in Frontier's 1966 "profit sharing."

By ignoring the loss in Frontier's case and including the loss in Petitioner's case, Respondent discriminated against Petitioner, and Petitioner was denied the equal treatment required by the Fifth Amendment, inasmuch as there was no rational basis for the distinction. **H.C.&D. Moving & Storage Co., Inc., et al. v. United States, et al.**, D. C. Hawaii, 298 F. Supp. 746, 751 (4).

4. There is now pending before the United States Court of Appeals for the Fourth Circuit the case of Allegheny Airlines, Inc. v. Civil Aeronautics Board, No. 14,892, and there is pending before the United States Court of Appeals for the District of Columbia Circuit the case of Texas International Airlines, Inc. v. Civil Aeronautics

Board, No. 24459. The Allegheny case was heard before the Court of Appeals on June 9, 1971, and the Texas International case was heard before the Court of Appeals on September 17, 1971, but as of the filing of this Petition, no decision has been rendered in either case.

Like Petitioner, both Allegheny and Texas International were required to refund a portion of the subsidy they had received for 1966, based on later year tax loss carrybacks. Their appeals now pending are, in almost every respect, identical with the appeal which the Court of Appeals for the Eighth Circuit decided adversely to Petitioner and which occasions this Petition for Writ of Certiorari.

CONCLUSION

It is, therefore, entirely possible that the decision in the Allegheny or Texas International case, now pending before the respective Courts of Appeals will be in conflict with the decision rendered in the Eighth Circuit in the case of the Petitioner. Should such a conflict become apparent, Petitioner respectfully submits that Certiorari should be granted pursuant to Supreme Court Rule 19 (1) (b).

Respectfully submitted

NEALE, NEWMAN, BRADSHAW & FREEMAN

PAUL L. BRADSHAW
705 Woodruff Building
Springfield, Missouri
Attorneys for Petitioner, Ozark Air Lines, Inc.

APPENDIX A

Order 10-5-107

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Adopted by the Civil Aeronautics Board
at its office in Washington, D. C.
on the 21st day of May, 1970

LOCAL SERVICE CLASS SUBSIDY RATE (OZARK AIR LINES, INC. SUBSIDY REFUND—1966)	Dockets 16750 and 15359

ORDER DETERMINING SUBSIDY REFUND

In this order the Board has determined, pursuant to the provisions of Class Rate III-A,[1] that Ozark Air Lines, Inc. shall refund $246,579 of subsidy for calendar year 1966. Since $95,621 has already been withheld by the Board, the net refund required will be $150,958.

The history, background and general nature of class rate profit-sharing determinations have been thoroughly canvassed and explained in numerous Board orders determining subsidy refunds for local service carriers.[2] For present purposes, it is sufficient to state that Class Rate

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[1] Orders E-23697, May 18, 1966, and E-23850, June 23, 1966.

[2] See *e.g.*, Ozark Air Lines, Inc. Subsidy Refund 1963-1964, Order E-25553, August 18, 1967, and Subsidy Refund 1965, Order 69-1-129, January 30, 1969.

III-A, like most of the other class rates,[3] under certain conditions requires refunds of a portion of the subsidy paid; that the refunds are to be made in accordance with the detailed profit-sharing provisions of the rate formula; and that a special report, Form T-88, must be submitted by each local service carrier in order to facilitate the profit-sharing and subsidy refund calculations. The administration of profit-sharing and subsidy refunds does not involve rate-making determinations and the profit-sharing provisions of Class Rate III are final, are not open to contest retroactively, and are not in issue.

On May 12, 1967, Ozark submitted Form T-88 in connection with the determination of profit-sharing for 1966. In accordance with established practice, the Form T-88 has been subjected to field audit by the Board's staff at the site of the carrier's operations, and a staff report of the audit findings has been made to the Board. Upon review of the audit report, the carrier's Form 41 reports, the data contained in the carrier's T-88 report, and the supplemental materials developed in communications and discussions between Ozark and the Board's staff, we have concluded that under the terms of Class Rate III-A Ozark shall refund $246,579 in subsidy for calendar year 1966.

The Form T-88 submitted by the carrier for 1966 conforms to, and is consistent with, the requirements of the class rate, except in the following respects:

1. Section III B 1 requires that expenses be consistent with the reporting requirements of the Federal Aviation Act and the Board's regulations. Pursuant to this section, we have made the following adjustments:

---

[3] Under Class Rate IV, Orders E-25162, May 17, 1967, and E-25231, June 1, 1967, a revenue-growth adjustment reduction factor has replaced the profit-sharing provisions of prior class rates.

a. We have eliminated from expense a credit of $20,969 relating to an overaccrual of payroll taxes in 1965, which was reflected in the 1965 profit-sharing determination.

b. Ozark amortized prepaid rent on leased aircraft and engines on the basis of a three-year lease, although, with option clauses granting the carrier the right to extend the lease for a period of five years, the lease had a life of eight years. Consistent with Board regulations the carrier should have amortized the prepaid rent over the entire life of the lease. We have therefore adjusted the amortization period and disallowed $14,856 of amortization.

2. Pursuant to section III B 4 various adjustments have been made to reflect the correct amortization of developmental and preoperating costs resulting in a net disallowance of $2,078 from the carrier's claim.

3. Consistent with our actual tax policy, as reaffirmed in Order 70-3-92, March 18, 1970, and in accordance with the requirements of section III E, we have adjusted federal income taxes for 1966, reported by Ozark on its Form T-88, to reflect the carryback of 1969 net operating losses. As a result, no provision has been made for federal income taxes for 1966 profit-sharing. However, since the various state tax laws make no provision for operating loss carrybacks, we have provided for taxes as reported by Ozark on its state tax returns, adjusted to eliminate $5,028 of taxes applicable to capital gains on flight equipment excluded from income for profit-sharing.

4. Pursuant to section III F, the Board has made appropriate adjustments to the carrier's Form T-88 investment to reflect the various revenue and expense adjustments set forth above. In addition, the following adjustments to investment have been made:

a. Section III C 2 f requires that investment shall not include equipment purchase deposits, and specifications in Schedule W of Form T-88 require that such deposits be eliminated from investment on a *pro rata* basis. The carrier instead of eliminating $3,463,902 of special deposits from investment on a *pro rata* basis, excluded the entire amount from debt investment. We have therefore adjusted the carrier's T-88 by (1) increasing average debt investment by $2,467,337, (2) excluding $1,211,673 from average convertible debenture investment, and (3) excluding $1,255,664 from average equity investment.

We have also adjusted the carrier's entry of $83,559 of average capitalized interest on special equipment deposits by excluding that amount from investment on a *pro rata* basis, whereas the carrier eliminated this amount entirely from debt investment. The net effect of our adjustment is that average debt investment is increased by $59,519 while average convertible debenture investment and average equity investment are reduced by $29,229 and $30,290, respectively.

The carrier did not exclude from investment the funds which had been recorded as a current asset but which more properly should have been recorded as a special deposit. Accordingly, pursuant to section III C 2 f we have eliminated $48,695 from *pro rata* investment.

b. Equity has been reduced by an average of $105,945 to reflect the portion of Ozark's liability for 1964 and 1965 profit-sharing (after taxes) which was not reflected in the carrier's reports for 1966.

c. Investment has been decreased by an average of $5,334 reflecting costs incurred in unsuccessful route cases not eliminated from the carrier's T-88 investment.

d. Section III C 2 b requires nonoperating property to be eliminated from investment on a *pro rata* basis.

The carrier did not exclude from investment the value of nine DC-3 aircraft, which had been taken out of service. We have therefore reduced average *pro rata* investment by $32,653.

e. Average equity investment has been increased by $218,689 to reflect the carrier's actual income tax liability for 1966, after giving effect to refunds resulting from the carryback of a 1967 investment tax credit and to reflect a carryback of net operating losses from 1969.

With the revisions indicated above,[4] and after reflecting the impact of such revisions in the related calculations under the formula, the amount of subsidy refund due from Ozark Air Lines, Inc., for the calendar year 1966 is determined to be $246,579.

Accordingly, It Is Ordered That: Ozark Air Lines, Inc. shall refund $246,579 to the Government for the calendar year 1966 pursuant to Class Rate III-A.

By the Civil Aeronautics Board:

Harry J. Zink
Secretary

(Seal)

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[4] In addition to the revisions and adjustments discussed above, other minor adjustments of a miscellaneous and routine nature have been made, but none of them are of sufficient consequence either individually or collectively to warrant discussion herein.

APPENDIX B

United States Court of Appeals
FOR THE EIGHTH CIRCUIT

No. 20,543

Ozark Air Lines, Inc., Petitioner,
v.
Civil Aeronautics Board, Respondent.
} On Petition for Review of Orders of the Civil Aeronautics Board.

[May 5, 1971.]

Before ALDRICH,* LAY and BRIGHT, Circuit Judges.

ALDRICH, Circuit Judge.

This dispute between Ozark Air Lines, Inc. and the Civil Aeronautics Board can be reduced to a relatively simple basic issue. Ozark, and a number of other so-called local service airlines in other parts of the country, for years have required subsidization, determined by "need." Federal Aviation Act of 1958, as amended, 49 U.S.C. § 1376(b). Prior to 1961 this was effected on an individual basis, but the resulting problems led to the adoption of a

* Of the First Circuit, sitting by designation.

uniform rate structure. See Local-Service Class Subsidy Rate Investigation, 34 C.A.B. 416 (1961). This general formula was altered from time to time. For the year 1966 it was known as Class Rate III-A. Investigation of the Local Service Class Subsidy Rate, Orders E-23697, May 18, 1966, and E-23850, June 23, 1966. This required, if operations proved to be profitable after taxes, a partial repayment of the subsidy, to effect profit sharing between the airline and the government. Taxes were to be those reported, "with such amendments and revisions *as may have been filed* as of the final determination of profit sharing hereunder." (Emphasis added.)[1] Ozark made a profit in 1966, and incurred a tax. In 1969 it operated at a loss. This gave it a loss carry-back, which could be used to reduce its 1966 tax, and hence increase its 1966 profit as measured under the order. The Board, still in the process of determining the amount of profit-sharing for 1966 when the information for 1969 became available, calculated the tax adjustment to which Ozark was entitled, and therefore required a larger profit-sharing refund to the government. Local Service Class Subsidy Rate, Subsidy Refunds, Order 70-3-92, March 18, 1970; Order Determining Subsidy Refund Order 70-5-107 May 21, 1970. Ozark objects.

Ozark's complaint is that the Board had no right to consider its potential tax reduction in 1966 resulting from the 1969 losses. Its first reason is that when the Board took March 18, 1970 as the final determination date for the refund due from 1966, Ozark's tax return for 1969, showing a loss, had not in fact been filed, Ozark having obtained an extension of the March 15 filing date. Consequently, Ozark says, even if the Board could properly take March 18, 1970 as the date of final determination of

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[1] Investigation of the Local Service Class Subsidy Rate, Order E-23850, June 23, 1966, § III-E-1.

profit sharing, by considering a return that had not yet "been filed" it departed from the terms of the general order, quoted ante. To this the Board replies that all of the information it used had already been supplied in reports that Ozark had been obliged to file with it, including a "pro forma" tax return, the correctness of which Ozark concedes. These reports, the Board found, showed that the tax credit would in fact be claimed. Hence, for Ozark to escape the consequences of its known, actual tax credits by the simple process of obtaining the consent of the Internal Revenue Service not to file on time, even if done in good faith and for other purposes, would be to "ignore reality." We cannot but agree. This is a case for the application of the rule that if literal use of language leads to "absurd results" in the light of a provision's obvious purpose, the purpose must control. *United States* v. *American Trucking Ass'ns, Inc.*, 1940, 310 U.S. 534, 543-44. Ozark's "need" of a subsidy is not to be determined by formalisms.

Alternatively, Ozark contends that the Board improperly selected March 18, 1970 as the date of final determination of the 1966 profit sharing, and that if an earlier settlement date had been selected its carryback loss would not have accrued and its net profit for 1966, in which the government was entitled to share, would not have been enhanced. More exactly, at an earlier date the parties would not have known that the profit was going to be enhanced by a tax reduction derived from net losses in 1969, and the Board, by closing the books, would have foreclosed the government's right to share in the increased profits when in due course they utimately accrued.

Ozark's argument for "ignoring reality" in this respect is somewhat more sophisticated but, we believe, equally fallacious. It is true, as Ozark points out, that consistent with orderly procedure, the Board attempts to make a

final determination with respect to each year—and each airline—as promptly as possible, and that benefits accruing after the final determination need not then be shared with the government.[2] With regard to 1966 a dispute arose between Ozark and the Board's staff as to an unrelated matter affecting the profit-sharing determination, which greatly postponed the settlement date. But for this dispute there would have been a final settlement before the 1969 losses occurred and generated the carryback, and Ozark would have been able to retain the entire increase. The difficulty with this argument is that while application of Class Rate III-A could result in windfalls, it adopted an "actual tax" policy[3] under which the Board computed the tax as accurately as possible on the basis of the facts as known at the time that all other disputes were resolved and the case was ready for closing. It looks to the true facts, in other words, in each case, so far as it is possible to determine them, without speculating, and without delaying longer than other circumstances require.[4]

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[2] This follows from the language of Class Rate III-A, as quoted ante.

[3] *Western Air Lines, Inc., and Inland Air Lines, Inc., Mail Rates,* 14 C.A.B. 243, 251-55 (1951), *aff'd in relevant part sub nom. Summerfield v. CAB,* 207 F.2d 200, *aff'd sub nom. Western Air Lines, Inc. v. CAB,* 347 U.S. 67.

[4] We can do no better than quote the Board.

> "The Board is here applying a policy it has consistently applied to all carriers similarly situated. That policy is to predicate the tax allowances on the basis of the carrier's actual income tax liability so far as it is known at the time of the Board determination. The Board has always been aware of the fact that in the normal course of administration of tax laws, the carrier's taxes for a given year are subject to change after our determination has been made final. But it would be totally infeasible to attempt to hold open each case until all possibility of amendment to the carrier's tax returns for that year had passed. Taxes can be affected by carryback credits, by voluntary amendments of returns by the taxpayers, and by deficiency assessment of the Internal Revenue Service, and were we to deter our final action on return and profit-

This practice not only seems reasonable, it costs the airline nothing in terms of the true facts. All that Ozark can say is that had the formula provided for an earlier fixed date, or had there not been in this case another dispute, it would have received a windfall. We see nothing arbitrary about this loss. Nor does the circumstance that the Board ultimately overruled its staff, so that Ozark won the other dispute, call for a different result. There is no suggestion that the staff was acting other than in good faith.[5] That the staff proved to be wrong no more calls for ignoring the then-known realities of Ozark's tax position than does the fact that Ozark chose to delay the filing of its tax return.

Finally, Ozark contends that the Board's selecting a different date for it than for some other lines[6] enjoying

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sharing matters until the various statutory limitation periods expired, it would be virtually impossible to maintain carriers on a current rate status and there would be continual uncertainty as to the government's obligations under section 406, as well as uncertainty as to the carrier's revenues. It is for these reasons that the Board has followed the practice of relying upon the tax returns on file as of the date of finalization of the rate or profit-sharing case. In this manner, both the carrier and the Board are bound to the facts then existing. Subsequent changes in the tax allowance may work to the carrier's benefit or to its detriment, and the carrier takes the risk that a subsequent deficiency assessment by Internal Revenue Service will occur in a closed rate period and will not be underwritten under section 406. By the same token, tax refunds for the year become beyond our reach if they occur during a closed rate period."

Local Service Class Subsidy Rate, Subsidy Refunds, ante.

[5] Ozark states in its brief,

"We recognize, of course, that all carriers cannot be processed simultaneously. And we do not claim that the Board has failed to act as expeditiously as possible under the circumstances or that the Board has intentionally processed the carriers in such order as to help or hurt any particular one."

[6] The March 18, 1970 order affected a number of local service carriers, but some others, with whom there had been less extensive disputes, had had their 1966 subsidies previously determined.

the benefits of Class Rate III-A subsidies caused inequalities in results, and was so arbitrary as to violate due process. This raises two questions: what are the disadvantages of a different rule governing the time of determination, and how serious is the occasional divergence in result called for by the present one. To take the second question first, while the matter was not gone into, Ozark conceded in oral argument that it was not in competition with the other local service airlines. There is hence no pressing obligation that in any particular year they should all receive equal treatment, so long as there is general fairness.

As to the alternatives open to the Board, Ozark has suggested two.

> "First. It could have delayed the final determination of any carrier's 1966 subsidy until all carriers had been processed so that simultaneous determinations could be made for all; . . ."

That all carriers should have to wait to know what their subsidies are to be until the last argument between the Board and the last carrier has been finally settled—it may be noted that after five years this one has not been settled yet—seems so unreasonable as to cause wonder why it should be advanced.

Ozark's second suggestion is that it would be fairer to have an arbitrarily fixed, identical, settlement date for all airlines as to the effect of taxes on the calculation of "profit." Certainly this would not help lines that had already reached agreement with the Board before that date had arrived to achieve the final certainty that all parties agree is desirable. Nor could it lead to early certainty with respect to other lines which, by hypothesis, were still engaged in disputes. Nor, in terms of windfalls, is it necessarily to an airline's advantage to have an

early settlement date. As the Board pointed out, n. 4, ante, the windfall, if any, resulting from an earlier settlement date may benefit the government. Had there been a tax deficiency established with respect to 1966 in this case, rather than a loss carryback, the carrier would have benefitted rather than lost by the delay. In this respect the "gamble" resulting from a differentiation in settlement dates, dictated by independently good reasons, is applicable to all alike. We see nothing illegal or arbitrary about Class Rate III-A, or the Board's procedure thereunder.

Affirmed.

A true copy.

Attest:

Clerk, U. S. Court of Appeals, Eighth Circuit.

APPENDIX C

United States Court of Appeals
For the Eighth Circuit

No. 20543 September Term, 1970

Ozark Air Lines, Inc.,
Petitioner,
vs.
Civil Aeronautics Board,
Respondent.

On Petition for Review of Order of the Civil Aeronautics Board

Petition of petitioner for rehearing filed in this cause having been considered, it is now here ordered by this Court that the same be, and it is hereby, denied.

June 2, 1971

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No. 71-801

In the Supreme Court of the United States

OCTOBER TERM, 1971

OZARK AIR LINES, INC., PETITIONER

v.

CIVIL AERONAUTICS BOARD

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE CIVIL AERONAUTICS BOARD IN OPPOSITION

ROBERT H. BORK,
Solicitor General,
WALTER J. CUMMINGS,
Assistant Attorney General,
GERSHON M. ROSENBERG,
HARRY FINGER,
Attorneys,
Department of Justice,
Washington, D.C. 20530.

W. VERNON CHEEVER,
General Counsel,
A. J. MEIGHAN,
Deputy General Counsel,
WARREN L. DEAN, JR.,
Associate General Counsel,
Civil Aeronautics Board,
Washington, D.C. 20428.

In the Supreme Court of the United States

OCTOBER TERM, 1971

No. 71-601

OZARK AIR LINES, INC., PETITIONER

v.

CIVIL AERONAUTICS BOARD

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE CIVIL AERONAUTICS BOARD IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A-6 to A-12) is reported at 441 F.2d 892. The challenged order of the Board (Pet. App. A-1 to A-5) and the opinion of the Board deciding the issues controlling the challenged order (App., *infra*, pp. 11-23) are not yet reported.

JURISDICTION

The judgment of the court of appeals was entered on May 5, 1971, and a petition for rehearing was denied on June 2, 1971 (Pet. App. A-13). On August 19, 1971, Mr. Justice Blackmun extended the

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time for filing a petition for a writ of certiorari to October 30, 1971, and the petition was filed on that date. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1) and 49 U.S.C. 1486(f).

QUESTION PRESENTED

Whether, in the circumstances of this case, it was proper for the Civil Aeronautics Board, in calculating a subsidized air carrier's subsidy refund assessment for the year 1966, to take account of the carrier's 1969 tax loss carryback.

STATUTE AND REGULATION INVOLVED

Section 406(b) of the Federal Aviation Act of 1958, 72 Stat. 763, as amended, 49 U.S.C. 1376(b), provides in pertinent part:

> (b) In fixing and determining fair and reasonable rates of compensation under this section, the Board, considering the conditions peculiar to transportation by aircraft and to the particular air carrier or class of air carriers, may fix different rates for different air carriers or classes of air carriers, and different classes of service. In determining the rate in each case, the Board shall take into consideration, among other factors * * * (3) the need of each such air carrier * * * for compensation * * * sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for

> the commerce of the United States, the Postal Service, and the national defense. * * *

Section III–E of Civil Aeronautics Board Order E–23850, issued June 23, 1966, provides in pertinent part:

> 1. Federal and State income taxes shall be determined on the basis of the carrier's actual income taxes, including the reduction of taxes resulting from loss carrybacks and carryovers, as reported on its income tax returns submitted to taxing authorities for each year, with such amendments and revisions as may have been filed as of the final determination or profit-sharing hereunder; *Provided, however*, that, for the purposes of this order, the carrier's actual income taxes for a given review year will be adjusted to exclude taxes related to income which is not otherwise considered in the profit-sharing determination, hereunder, for that review year; *Provided, further*, that where a final profit-sharing determination for a prior period has been made and the tax basis relied upon in that final determination has been amended or revised subsequently, the effect of the change in taxes will be considered as income or expense for profit-sharing purposes in the year in which the change is made; * * *

STATEMENT

Under the Federal Aviation Act, 49 U.S.C. 1301, *et seq.*, petitioner and eight other local service air carriers are subsidized by the government to provide service to communities which do not generate sufficient traffic to permit unsubsidized service on an eco-

nomically sound basis. The amount of the subsidy is determined by the "need" of the carrier, see 49 U.S.C. 1376(b), *supra*, and the subsidy program is administered by the Civil Aeronautics Board. These subsidies were originally determined for each carrier on an individual basis, but after 1961 uniform class rates were established for all local service carriers. See *Local-Service Class Subsidy Rate Investigation*, 34 C.A.B. 416.

During 1966, the subsidy year involved in this case, Class Rate III–A was in effect. Like earlier Class Rates, it required carriers to share with the government profits in excess of specified levels. In calculating profits for this purpose, the carriers were to take account of their "actual income taxes, including the reduction of taxes resulting from loss carrybacks and carryovers." The Board's order further provided that these "actual income taxes" would be those taxes reported on the carriers' tax returns "with such amendments and revisions as may have been filed as of the final determination of profit-sharing hereunder." See Section III–E, Order E–23850 (*supra*, p. 3).

In accord with applicable regulations, petitioner submitted a profit-sharing report to the Board for 1966. A dispute then arose between petitioner and the Board's staff over the proper treatment of certain capital gains realized by petitioner. Petitioner asked to be heard by the Board, and on March 18, 1970, the Board issued an opinion (App., *infra*, pp. 11–23) agreeing with petitioner's position.

In that same opinion, the Board also dealt with several other issues raised by petitioner, as well as by five other carriers. As here relevant, the Board noted that the carriers' tax returns for 1969 were due on March 15, 1970, a date just past, but that the carriers, in accordance with their practice, had obtained extensions and had not yet filed their returns; had they been filed, the returns would have reflected loss carryback credits from 1969 against taxes paid in 1966—the profit-sharing year in question before the Board. No factual doubts were present as to the existence of losses in 1969 or the availability of loss carryback credits; the carriers' financial reports to the Board and their own admissions established these facts. The carriers had contended, however, that since the Board provided that tax allowances would be based on "tax returns submitted to taxing authorities," the Board could not take into account the loss carryback credit against taxes paid in 1966 because the carriers had not yet filed their returns (App., *infra*, p. 19). In response, the Board stated that "to accept such an argument is to ignore reality at the expense of the U.S. Treasury." It pointed out that 1969 was over and that the reports filed with the Board "disclose that such credits will in fact be claimed." The Board concluded that it "cannot in good conscience permit the tax allowance [of a carrier] to be affected by a matter so wholly within the control of the carriers as a request for an extension to file their income tax returns." Accordingly, the Board decided "to finalize profit-sharing

for the year 1966 on the basis of either a *pro forma* tax return for 1969, or a copy of the actual return as filed with [the] Internal Revenue Service" (App., *infra*, pp. 19–20).

The Board then turned to the carriers' contention that they were subjected to unlawful discrimination because, in some instances, other local service carriers had their profit-sharing for the years under consideration finally determined prior to the filing of their tax returns embodying loss carryback credits, and consequently the share of profits found to be owing to the government did not take these tax credits into account. In rejecting this argument, the Board pointed out that it has consistently followed a policy of assessing a carrier's tax liabilities as of the time it finally determines the amount of refund owed. To await all possible tax changes would require holding open each carrier's case for a far longer time than would be administratively feasible. There was no claim that the Board had processed the carriers in an arbitrary order, or that the Board had not attempted to dispose of each case as expeditiously as possible. Given its resources, the Board concluded, "some cases must be processed before others, and if in this particular instance some carriers have benefited from the fact that their cases were completed more promptly than others, that fact would not warrant us in providing an excessive tax allowance for the carriers whose cases are still before us" (App. *infra*, p. 22).

On May 21, 1970, the Board applied the above opinion to the facts of petitioner's case (Pet. App. A–1 to A–5).

On petition for review, the court below unanimously upheld the Board's action (Pet. App. A–6 to A–12). It agreed with the Board that it was proper to take into account petitioner's 1969 tax loss carryback, since there was no doubt that petitioner's *pro forma* return was accurate and since petitioner had not filed its official return only because the Internal Revenue Service consented to a late filing. To apply the Board's rules with undue literalness, the court noted, would, in light of their "obvious purpose," lead to "absurd results" (Pet. App. A–8).

The court also rejected petitioner's claim that it had been unfairly discriminated against. Under the Board's system, the amount of profits that each carrier was required to turn over to the government was determined on the basis of the actual facts known at the time of determination. Later events might work to the government's—or to the carrier's—advantage. This "gamble," the court stated, was "applicable to all alike" (Pet. App. A–12). Accordingly, the court concluded that there was "nothing illegal or arbitrary about Class Rate III–A, or the Board's procedure thereunder" (*ibid.*).

ARGUMENT

1. Petitioner contends (Pet. 8) that the Board discriminated against it in violation of the Fifth Amendment and the Administrative Procedure Act by utilizing its 1969 losses to determine 1966 profit-sharing, while not doing so for other carriers. This argument is without merit. In every profit-sharing

case, the Board utilized actual or *pro forma* tax returns filed or due to be filed by the carrier at the time the Board made its final profit-sharing determination. If, as in the case of petitioner and others, 1969 tax returns were available when 1966 profit-sharing obligations were determined, the returns were used in that determination. On the other hand, if, as in the case of Frontier Airlines (Pet. 9) and some other carriers, the 1966 profit-sharing determination was made before the 1969 tax return was even due, then it could not be utilized. Thus, all carriers similarly situated *at the time of decision* were treated the same, in accordance with the provisions of Class Rate III–A, *supra*, p. 3.[1]

2. Petitioner also contends (Pet. 8–9) that its 1969 losses should not have been taken into consideration because the Class Rate contemplated only the use of "tax returns submitted to taxing authorities" rather than the *pro forma* return used by the Board in petitioner's case. This argument, based on an unduly literal reading of the Class Rate, rather than its plain intent, is unpersuasive. As the Board noted, the normal due date for the tax returns was past, the facts were known and set forth in reports already filed with the Board, and the carrier's loss and the availability of the tax credits were established. The Board was certainly justified in not allowing petitioner to reap a windfall simply because it obtained

[1] Petitioner's objection that there was "no uniform date as to when losses would no longer be considered for subsidy purposes" (Pet. 8) is in reality a challenge to Class Rate III, whose provisions are final and not open to retroactive challenge (see Pet. App. A–2).

the consent of the Internal Revenue Service not to file its formal return on time. The court of appeals noted correctly that the Board's rules do not require such an "absurd result" (Pet. App. A–8). See *United States* v. *American Trucking Ass'ns., Inc.*, 310 U.S. 534, 543–544.

3. Petitioner points out (Pet. 9–10) that there are other cases pending in different courts of appeals which raise issues almost identical to the ones raised in this case. That fact, however, does not in itself warrant review of the decision below by this Court, since there is presently no conflict among the circuits, and it is impossible to say when, or if, such a conflict might occur.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted.

ERWIN N. GRISWOLD,
Solicitor General.
WALKER B. COMEGYS,
Acting Assistant Attorney General.
GREGORY B. HOVENDON,
HARRY FIRST,
Attorneys.

R. TENNEY JOHNSON,
General Counsel,
O. D. OZMENT,
Deputy General Counsel,
WARREN L. SHARFMAN,
Associate General Counsel,
Civil Aeronautics Board.

DECEMBER 1971.

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APPENDIX

United States of America

Civil Aeronautics Board

Washington, D.C.

Dockets 15359 and 16750

LOCAL SERVICE CLASS SUBSIDY RATE SUBSIDY REFUNDS

Allegheny Airlines, 1965–6
Lake Central, 1965
Ozark, 1966
Pacific, 1964–5
Texas International, 1966
West Coast, 1965–6

Decided: March 18, 1970.

Tax allowances for purposes of computing profit-sharing under Class Rates III and III–A for years 1964–6 should reflect the effect of credits relating to operating losses incurred under Class Rate IV in 1967–9 which were carried back for tax purposes to 1964–6.

The amount of the credits actually realized by the carriers resulting from operating loss carrybacks should not be increased to reflect capital gains realized under Class Rate IV.

OPINION

By the Board

The captioned proceedings involve the determination of the proper amounts owed to the government

for the years 1964–1966 by the subject carriers under the profit-sharing provisions of Class Rates III [1] and III–A.[2] Common to all of the cases are certain issues relating to the treatment of loss carryback tax credits generated by operations in 1967, 1968, and 1969. The broad question presented is whether or not the applicable provisions of the class rate orders require that these credits be taken into account in determining the amount of tax allowance for profit-sharing purposes in 1964–66.

Because of the importance of the issues raised, the Board afforded the carriers an opportunity to present their views on the issues in writing to the Board. In addition, representatives of the carriers made an o l presentation to the Board. The Board, having considered all matters presented to it, has made its determinations as to the proper treatment of the items in question and in the interest of the orderly processing of the individual profit-sharing cases, has determined to issue this order embodying its decision and the reasons therefor at this time.

I

From the inception of the local service class rate in 1961,[3] and through calendar year 1966, each local service class rate contained two basic elements: a formula providing for the payment of gross subsidy in which the amount of gross subsidy varied with the carrier's volume of operations and other factors as

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[1] 41 C.A.B. 138, 139, (1964).

[2] Orders E–23697, May 18, 1966, and E–23850, June 23, 1966.

[3] By Order E–16173, December 23, 1960, the Board instituted a proceeding directed to the establishment of a local service class subsidy rate. Class Rate I was established in 34 C.A.B. 416, 418 (1961).

specified in the formula; and a profit-sharing provision under which the carrier refunded a portion of the gross subsidy payment if its actual return on investment exceeded a defined level.[4] Effective January 1, 1967, the Board established Class Rate IV,[5] which, with certain modifications not here pertinent, is still in effect. Class Rate IV eliminated profit-sharing, and substituted a revenue growth-sharing formula under which the gross subsidy was reduced by a percentage of the annual growth in the carrier's gross passenger revenues. Under the revenue growth adjustment, subsidy is reduced irrespective of the over-all net profit position of the carriers.

We are here concerned solely with profit-sharing under Class Rates III and III–A for the years 1964 through 1966. However, the issue presented involves the treatment of certain operating losses realized, or to be realized, by the carriers in the years 1967 through 1969 while they were operating under Class Rate IV. These losses are carried back under the internal revenue laws to 1964 through 1966, thus reducing or eliminating the carriers' taxes in those years. The position of the Board's staff is that the resulting tax credits should be taken into account to reduce the allowance for the carriers' taxes to that shown on the carriers' actual income tax returns filed as amended for the years 1964 through 1966, whereas the carriers contend that they should be

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[4] In general, the recognized rate of return for each carrier is determined by applying the specified percentage rates to the carrier's debt and equity components, subject to certain minimum and maximum over-all rates of return. The provisions require a refund to the Board of 50% of the profit between the recognized rate of return and the return of 15% on investment and 75% of profits in excess of a return of 15% on investment.

[5] Orders E–25182, May 17, 1967, and E–25231, June 1, 1967.

allowed to retain the benefit of the tax credits as an amelioration of the losses incurred under Class Rate IV. We find that we are in agreement with the staff on this basic question for the reasons set forth below.

II

The class rate orders contain detailed provisions as to how revenues, expenses, investment, and income taxes shall be calculated for purposes of determining the amount of profit to be refunded to the Government. The provision regarding income taxes is set forth in section III–E, and so far as pertinent reads as follows:

> "1. Federal and State income taxes shall be determined on the basis of *the carrier's actual income taxes, including the reduction of taxes resulting from loss carrybacks and carryovers* and from investment tax credits, as reported on its income tax returns submitted to taxing authorities for each year, with such amendments and revisions as may have been filed as of the final determination of profit-sharing hereunder * * *"[6] [Emphasis added.]

This provision is clear and unambiguous. On its face, it requires that any losses carried forward from earlier years or carried back from later years, which reduce the actual income taxes paid for the profit-sharing year under review, must, for profit-sharing purposes, be used to reduce the carrier's tax allowance for that year.

We do not understand that there is any dispute as to the literal meaning of section III–E. It is argued, however, that section III–E was in effect modified by the adoption of Class Rate IV with the result that

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[6] 41 C.A.B. 138, 169 (1964); Order E–23850 June 23, 1966, page 22.

loss carryback credits generate under Class Rate IV may not be utilized by the Board in reducing the tax allowances for profit-sharing purposes for the years to which Class Rates III and III–A are applicable. We find the argument unpersuasive.

To begin with, it must be emphasized that nothing in Class Rate IV dealt with the question of loss carryback credits. There is not the slightest suggestion in that order to support the contention that the Board intended to repeal or modify any part of the profit-sharing provisions of Class Rates III and III–A. Therefore, the argument that Class Rate IV amended Class Rates III and III–A must necessarily rest on the proposition that the substitution of the revenue growth formula for the profit-sharing formula is so inconsistent with the continued applicability of the loss carryback tax provisions of Class Rates III and III–A as to have effected a *pro tanto* repeal. That proposition cannot be established.

The carriers variously argue that had the Board not substituted the revenue growth adjustment in Class Rate IV for profit-sharing, the losses incurred under Class Rate IV would have been substantially reduced, because in the absence of excess profits there would have been no profit-sharing refund to the Government. Since the refund under the revenue growth adjustment does not depend upon the profit status of the carrier, it is argued that carriers who incurred losses under Class Rate IV are penalized twice: once by having to refund a portion of their revenue growth to the government, and second by having the tax credits related to their losses applied to reduce prior subsidy rather than to ameliorate the losses. The argument boils down to the claim that, having sustained losses which were not underwritten by subsidy under Class Rate IV, the carriers are entitled to re-

tain the benefit of the tax credits which those losses generated.

The surface plausibility of the argument does not in our judgment withstand close scrutiny. The short of the matter is that the position of the carriers is at war with the Board's actual tax policy as it has been administered for almost 20 years. We find nothing in the adoption of Class Rate IV which would lend any solid measure of support to the contention that we intended to modify this policy of long-standing, or indeed that it would have been sound for us to do so, and we conclude that no such modification occurred.

Since the decision in the *Western Inland Mail Rate Case* in 1951,[7] the Board has adhered to the policy that the determination of tax allowances for purposes of subsidy under section 406(b) of the Act should be based on the carrier's actual income taxes as reflected on its tax returns filed with the Internal Revenue Service. The Board was there met with the contention of the carriers that taxes should be constructed on the assumption that the net taxable income for tax purposes was identical to the profit for return purposes (except for the tax reduction for return on indebtedness). As here, the carriers argued that the actual tax method "punished" them twice: once through disallowance of expenses incurred but not recognizable for rate-making purposes, and secondly by depriving them of the benefits of the tax deductions which the tax law allows. In the Board's view, however, calculating the carrier's taxes without regard to deductions and credits actually realized would result in paying to the carrier greater tax allowances than it actually incurred, and the Board considered "such allowances gratuities which we can no longer tolerate."[7a] Rather,

[7] 14 C.A.B. 243 (1951).

[7a] 14 C.A.B. at 253.

the Board emphasized that the function of the allowance for Federal income taxes is simply to insure that the carrier receives compensation for its income taxes as a cost of doing business. The allowance "is not designed to guarantee that the carrier will receive a gratuity or bonus which it can use to offset other losses. An allowance greater than the actual tax liability affords such a gratuity and should be avoided if possible."[8] Thus, the carriers' basic contention here, that they should be permitted to retain the benefit of the tax credits as a cushion for losses incurred but not underwritten by the Board, was specifically rejected in the *Western* case.

On the basis of the above policy, no tax allowance was in fact made for Western in the *Western Mail Rate Case* because, as a result of loss carryback credits, the carrier had no tax liability for the entire four-year period under review in that case. While the tax loss carrybacks in that particular case were related to losses incurred during the open rate period, the principle established was clearly applicable whenever loss carryforwards or carrybacks reduce the actual income tax liability for any year under review, and the Board has ever since reduced the tax allowances by the amounts of credits actually utilized by the carrier on its income tax returns for open rate periods irrespective of the fact that its credits may have related to losses incurred in closed rate periods.[9]

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[8] *Ibid.*, at 252.

[9] See, *e.g.*, Ozark Air Lines, Inc., Mail Rates, 32 C.A.B. 470, 474 (1960); Alaska Coastal-Ellis Airlines, Mail Rates, 40 C.A.B. 371, 376, 377, 379 (1964); Alaska Airlines, Inc., Mail Rates, 24 C.A.B. 273, 278 (1956); Trans-Pacific Airlines, Ltd., Mail Rates, 14 C.A.B. 273, 279 (1951).

And when the Board came to prescribing the method of computed tax allowances for purposes of profit-sharing under the class rate, it specifically incorporated this established policy that the allowable taxes shall not exceed the actual taxes as reflected in the carrier's returns, including loss carrybacks and carryforwards. It would take a far more persuasive showing than that before us to convince us that we unwittingly abandoned this policy with Class Rate IV.[10]

Accordingly, we conclude that section III–E requires the reflection of loss carryback credits which the carrier has used on returns filed with the Internal Revenue Service to reduce its taxes for the profit-sharing years under review.

III

The foregoing determination disposes of the broad issue as it affects the tax loss carrybacks from 1967 and 1968. However, a separate issue is raised with respect to 1969. The carriers' tax returns for the calendar year 1969 are due under the tax laws on March 15, 1970. However, the carriers have advised us that they will seek permission from the Internal Revenue Service to file their returns late, which is alleged to be consistent with their past practice. Thus,

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[10] The argument that the Board is legally barred from reaching losses generated under Class Rate IV because Class Rate IV is an independent and final rate is without merit. The allowances for taxes are clearly and unambiguously set forth in Class Rates III and III–A, which were in effect for the periods under review. Indeed, the converse of the carriers' argument would appear to be more accurate, namely that failure to reflect the carrier's actual income taxes, including these carryback credits, would involve a retroactive amendment to the class rate order which is barred by the principle of Transcontinental & Western Air Lines, Inc. v. C.A.B., 336 U.S. 601 (1949).

as of the date of the issuance of this order, it does not appear that the carriers have in fact filed their income tax returns covering 1969, and consequently have not reflected any loss carryback credits from 1969 against taxes paid for 1966, a profit-sharing year. Nevertheless, it appears from the air carriers' financial reports filed with the Board, and the carriers themselves acknowledge, that they will in fact have significant loss carrybacks related to the 1969 tax year which will be available to reduce or totally eliminate their tax liabilites for 1966. Notwthstanding the foregoing, the carriers urge that the computation of the tax allowance for profit-sharing purposes should not take into account these credits. The carriers argue that however we may dispose of the issue as it relates to 1967 and 1968 credits, 1969 stands on a different footing. They point to the fact that section III–E–1 specifically provides that the tax allowances shall be based upon the "tax returns submitted to taxing authorities for each year, with such amendments and revisions as may have been filed as of the final determination of profit-sharing hereunder . . ." It is thus contended that a literal application of the foregoing provision would not support the reduction of tax allowances on the basis of credits anticipated but not embodied in filed tax returns.

But to accept such an argument is to ignore reality at the expense of the U.S. Treasury. Under the quoted provision, as well as under our administrative practice, the Board takes the tax returns as it finds them, and does not attempt to project taxes as they may appear on returns to be filed in the future. Here, however, the fact that the carriers will realize substantial tax credits is no longer a matter of forecast. Their Form 41 reports for the calendar year 1969

have been filed and disclose that such credits will in fact be claimed. The carriers do not dispute this. Moreover, had the carriers filed their returns on March 15, as provided by statute, section III–E–1 would require us to take into account the credits. The Board cannot in good conscience permit the tax allowance to be affected by a matter so wholly within the control of the carriers as a request for an extension to file their income tax returns. We do not, of course, mean to question the carriers' motives in seeking an extension of time from Internal Revenue Service. But by the same token, the grant of such an extension cannot be accepted as the basis for a tax allowance, which is patently in excess of the carriers' actual taxes. In view of the foregoing, the Board has determined to finalize profit-sharing for the year 1966 on the basis of either a *pro forma* tax return for 1969, or a copy of the actual return as filed with Internal Revenue Service.

IV

In reaching the foregoing determinations, we have considered the carriers' arguments that they are being subjected to discrimination because, in some instances, other local service carriers had their profit-sharing for these years established prior to the filing of their tax returns embodying loss carryback credits, and tax allowances for profit-sharing purposes therefore did not take these credits into account. Since these determinations have been considered to be final, these carriers have in effect retained the benefit of the credits. The carriers' argument is similar to arguments based on administrative lag which the Board has considered and rejected.[11]

[11] National Airlines, Inc., Mail Rates, 18 C.A.B. 442 (1954).

The Board is here applying a policy it has consistently applied to all carriers similarly situated. That policy is to predicate the tax allowances on the basis of the carrier's actual income tax liability so far as it is known at the time of the Board determination. The Board has always been aware of the fact that in the normal course of administration of tax laws, the carrier's taxes for a given year are subject to change after our determination has been made final. But it would be totally infeasible to attempt to hold open each case until all possibility of amendment to the carrier's tax returns for that year had passed. Taxes can be affected by carryback credits, by voluntary amendments of returns by the taxpayer, and by deficiency assessment of the Internal Revenue Service, and were we to defer our final action on return and profit-sharing matters until the various statutory limitation periods expired, it would be virtually impossible to maintain carriers on a current rate status and there would be continual uncertainty as to the government's obligations under section 406, as well as uncertainty as to the carrier's revenues. It is for these reasons that the Board has followed the practice of relying upon the tax returns on file as of the date of finalization of the rate or profit-sharing case. In this manner, both the carrier and the Board are bound to the facts then existing. Subsequent changes in the tax allowance may work to the carrier's benefit or to its detriment, and the carrier takes the risk that a subsequent deficiency assessment by Internal Revenue Service will occur in a closed rate period and will not be underwritten under section 406. By the same token, tax refunds for the year become beyond our reach if they occur during a closed rate period.

The fact that some carriers' profit-sharing determinations were made final while the present carriers'

cases were still pending provides no basis for departing from our actual tax policy and the tax provisions of the class rate orders. There is no claim that the Board or its staff has acted in an arbitrary fashion in the order in which the cases have been processed, and the Board has in fact attempted to process all of these cases as expeditiously as possible consistent with its workload and resources. Nevertheless, some cases must be processed before others, and if in this particular instance some carriers have benefited from the fact that their cases were completed more promptly than others, that fact would not warrant us in providing an excessive tax allowance for the carriers whose cases are still before us.

V

We finally turn to an issue raised by the staff as to the effect of certain capital gains realized in 1968 by Ozark and Texas International. These gains are protected under the terms of section 406 (d) of the Act from offset against subsidy requirements.[12] The staff contends that since the carriers are in effect permitted to keep these gains, they should be charged with the taxes related to them. Since the carriers' income tax returns for 1966 indirectly reflect these capital gains, in the sense that the gains reduced the amount of the loss carryback credit, the staff proposes an adjustment to the tax returns so as to remove the impact of the gains on allowable taxes. However, the adjustment proposed is not supported by the language of the

[12] Section 406(d) provides in substance that capital gains realized upon a disposition of flight equipment shall not be considered in determining the need of the carrier for subsidy purposes if the gains are reinvested in other flight equipment.

class rate order.[13] Moreover, the adjustment is in our opinion not consistent with the principle underlying the loss carryback provision, as well as with our affirmance herein of the policy that taxes shall be based upon actual taxes. Having determined that the loss carryback credit should be reflected in the tax allowance notwithstanding the fact that the losses occurred in a closed rate period, it would be inconsistent for us not to take into account an offset to the credit which the carrier by law is required to make, on the ground that it relates to a gain which is not recognized for subsidy purposes.

Appropriate orders embodying the foregoing determinations will be entered following completion of the processing of the individual profit-sharing cases.[14]

BROWNE, Chairman, GILLILLAND, Vice Chairman, MINETTI, MURPHY, and ADAMS, Members, concurred in the above opinion.

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[13] Section III–E–1 provides that "the carrier's actual income taxes for a given review year will be adjusted to exclude taxes related to income which is not otherwise considered in the profit-sharing determination, hereunder, for that review year . . ." Under this provision, capital gains taxes related to gains realized in a profit-sharing year would be excluded for purposes of the profit-sharing determination.

[14] Certain other issues raised by the carriers will be disposed of in the processing of their individual profit-sharing cases.

U.S. GOVERNMENT PRINTING OFFICE: 1971